

1 Business

Exam practice answers

Some exam practice questions clearly ask for one (or occasionally two) answers. You will often see more answers than are required by the question. This is intended to illustrate the different ways in which a question can be tackled. It is **not** intended to suggest that you should offer more answers than are required by the question.

1.1 The purpose and nature of business

1. Opportunity cost is what is given up as a consequence of a particular decision.
2. Answers may include the following:
 - + Land resources would include a range of foods such as meat, vegetables and cooking oils as well as spices and herbs.
 - + Capital resources would include the building itself, cooking equipment and furniture such as tables and chairs for the restaurant dining area.
3. Answers may include the following:
 - + An increase in interest rates would mean that Rafael would have to pay more for his loan. This could make it more difficult for him to succeed – especially if he doesn't attract enough customers. If he does have enough customers and revenue, he may not be able to pay the increased interest costs of his loan and he may decide not to start the business.
 - + The size of the loan and the fact that interest rates are forecast to increase 'substantially' may be a big problem for Rafael. These two factors may mean that he has to pay a lot more interest to his bank and this might mean his business does not make a profit. Rafael is already worried about this, suggesting it is a major issue. This may cause him to change his plan and increase his prices.
4. Answers may include the following:
 - + There are some downsides. Rafael seems to lack some confidence and is concerned about his business's prospects, which suggests he may not be a natural risk-taker. This is reinforced by his wife's view that he is someone who worries a lot about money. As risk taking is a vital element of being a successful entrepreneur, it may be that Rafael would not be a good entrepreneur.
 - + However, Rafael is very keen on cooking, is creative and works hard at his ideas. These are important characteristics for an entrepreneur and could be essential given the type of business that Rafael intends to set up. This is supported by him being organised which would be vital to help him plan and carry out the challenging task of creating a new restaurant from scratch.
 - + Rafael has some of the characteristics of a successful entrepreneur but lacks one which may be most essential – that of being comfortable in taking a risk. He is worried about money and the possibility of losing his home. This is understandable but probably means he wouldn't be a natural entrepreneur and would be less likely to succeed in this role.

1.2 Business ownership

1. The Stock Exchange is a market for buying and selling shares of public limited companies.
2. Answers may include the following:
 - + A public limited company is a legal structure used for large businesses such as Marks & Spencer plc who have many employees and large numbers of customers. Paula's business will be much smaller.
 - + It is very expensive to establish a public limited company and although Paula is wealthy, she does not have sufficient money to start a plc – nor does she need to do so, as she doesn't need to sell shares to the general public to raise money to start her business.

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3. Answers may include the following:

- + The Deed of Partnership will set out the rules governing the business. Paula has clear ideas and she could ensure that she has the majority of the voting rights, so that she remains in control. This could be particularly important as she likes being in control and this would make the situation clear to a business partner.
- + Paula is quite wealthy and is likely to put a large sum of money into the business. The Deed of Partnership can set out what percentage of profits she would receive and make sure it reflects her investment and involvement. If she doesn't have a Deed of Partnership, her returns may not reflect the risk she is taking.

4. Answers may include the following:

- + Paula is a wealthy person and, if she establishes Bloomers as a private limited company, she will benefit from the protection of limited liability. This means that if the business fails – or incurs large debts – her personal possessions will not be used to pay the business's debts. This is vital given her financial position.
- + Paula is a decisive person and would enjoy operating her flower shop as a sole trader. This would allow her to make all of the decisions without the need to consult other people. Decisions could be made quickly which might help Paula to establish her new business.
- + On balance, Paula should choose to use a private limited company as the legal structure for her flower shop. The protection of limited liability is very important as she is wealthy and has no entrepreneurial experience. It would also allow her to benefit from her cousin's advice while still being able to make the final decision.

1.3 Setting business aims and objectives

1. Answers may include the following:

- + Profit maximisation
- + Growth
- + Survival

2.

Market share = value of one business's sales ÷ total value of sales in the market x 100

$$\text{Market share in Year 1} = \frac{£900,000}{£27,550,000} \times 100 = 3.27\%$$

$$\text{Market share in Year 2} = \frac{£2,450,000}{£36,700,000} \times 100 = 6.68\%$$

3. Answers may include the following:

- + Raj sells his products to a small number of large businesses. If he lost just one customer this could mean that he loses a large number of sales, and his profits could be substantially reduced as a result. This is one reason why Raj has set his customer satisfaction objective and seeks to achieve it by providing advice and excellent after-sales service which helps to keep his customers loyal.

4. Answers may include the following:

- + Raj's business has grown quickly and its sales have risen rapidly, nearly tripling in Year 2. His business appears popular perhaps because his prices are low. It might be possible for him to put his prices up and this would help him to make more profits.
- + Raj has been very successful so far and his business is still small. There is no reason for him to change his objective away from customer satisfaction when his customers are so important to

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the business's future. He does not know how his customers will respond to increased prices and raising them would be a risk.

- + Overall, there seems little reason for Raj to change his objectives at this point. The business is growing quickly – which is its aim – and it made a small profit in its second year. If he increases prices, its sales may not rise so quickly, leading to slower growth.

1.4 Stakeholders

1. Answers may include the following:

- + Owners
- + Employees
- + Customers

2. Answers may include the following:

- + A company's shareholders often want high profits to receive regular dividends. Lerwick Ltd's profits have been low for some time and the shareholders are becoming unhappy.
- + A company can raise money by selling more shares to its shareholders if they are satisfied with its performance. Usha will need to raise funds if her plans go ahead and if they are unhappy she may not be able to raise the finance she needs.

3. Answers may include the following:

- + The cut in prices may not increase the company's profits as Usha is doing this in 'the hope' of increasing profits. The company's shareholders may not agree that this is a good decision if they think that the company's customers will not buy more of its products.
On the other hand, Lerwick Ltd's customers will be delighted by this move. Retailers such as Argos may continue selling the fishing equipment at the same price and enjoy more profits.
- + Employees may be less happy with the cut in the company's prices. This could result in a wage cut, or at least make it much more difficult to negotiate a pay rise.
In contrast, the company's suppliers may be pleased if they think that this decision will result in higher sales by Lerwick Ltd and increased orders for their products.

4. Answers may include the following:

- + Moving the factory should result in lower costs to produce the company's fishing equipment. This might help it to increase its profits, especially as it has cut its prices. Lerwick Ltd's profits have been low for several years and action is probably needed. This would help to satisfy the shareholders.
- + Moving may lead to very poor relations with the company's employees. Some of them will lose their jobs to new technology, while others will have to move or travel 40 miles to the new factory. This may damage the company's performance as experienced employees may leave.
- + There is a financial pressure to move the factory to a lower-cost location. Usha has cut prices and she needs to keep costs as low as possible. This move may involve short-term problems, especially with employees, but could bring significant long-term benefits by satisfying both shareholders and customers.

1.5 Business location

1. Globalisation is the trend for many markets to become worldwide in scope.

2. Answers may include the following:

- + Harris plc sells its clothing at the lowest possible prices. This means it will want to find a location where costs such as rent are lower – this might be just off a high street rather than on it.

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- + The retailer sells its clothing mainly to young people aged 16–30. It is important for the business to locate in places where young people may shop – or at least pass by.
3. Answers may include the following:
- + Harris plc has been opening stores regularly since 2000. This might slow down or stop if the company decided to concentrate on selling more of its products online. It will probably not open any further small stores and any new ones that it does open will be large stores in cities.
 - + The company will have to open two new warehouses to supply products to its online customers. These will not be located in cities but probably in cheaper locations where there are good transport links, ideally near to motorways or other major roads. This will make it quicker and cheaper to send products to customers, possibly increasing sales and profits.
4. Answers may include the following:
- + The supplier will benefit from lower costs of production in India as wages and other production costs are likely to be much lower. This might help the supplier to sell its products more cheaply. This might help it to win more customers like Harris plc.
 - + Harris plc is a major customer of this supplier. Harris plc sells fast fashion, which has to be designed and produced very quickly. This might be more difficult if much of the supplier's production takes place in India and then has to be transported to the UK. Time is very important in this industry.
 - + Although the extra time involved in production might at first appear to be a problem for the supplier, India is a popular location for businesses manufacturing clothes and modern transportation is very quick. Price is important to customers such as Harris plc and so this could be a good move for the supplier.

1.6 Business planning

1. Profit measures the difference between the value of a business's revenue (from sales) and its total costs.
2. The total revenue of the business will be $£26,500 + £14,750 = £41,250$
- Total costs = $£7,450 + £19,950 = £27,400$
- Profit = $£41,250 - £27,400 = £13,850$
3. Answers may include the following:
- + Chris needs to borrow quite a lot of money to start his bicycle shop. His business plan suggested that he would need a loan of £25,000, which is about 40 per cent of the money required to start his business. Any bank considering lending him the money would expect to see a business plan to judge whether the money would be likely to be repaid. Without a plan he probably would not receive a loan.
 - + Chris is unsure whether he should start his business. Preparing a business plan will help him to understand more about his business and its chances of success. Once he has completed his business plan, he might be able to make a more informed decision on whether or not to go ahead with his enterprise. Thus, a business plan will reduce the level of risk he faces.
4. Answers may include the following:
- + Chris has no experience in running a business and this might mean that he makes some wrong decisions once he is managing the business. As a result, his business might not be a success and he may not make sufficient profit to repay the loan. The bank manager may think that this loan would be very risky.
 - + Chris is investing more than half the money that is required to start his business and is preparing a business plan to help him to make a judgement on whether or not he should go

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ahead. This should help to give the bank manager more confidence that Chris's business will be successful.

- + On balance the business's prospects look favourable. He is forecast to make a large profit in his first year and an accountant has helped him to prepare the financial forecasts. The profit figure is more likely to be accurate as a result and, if correct, suggests the business will be a financial success. The bank should grant the loan.

1.7 Expanding a business

1. Organic growth occurs when a business gets bigger by selling more of its products.

2.

Monthly output of product (items)	Total cost of production (£)	Average unit cost (£)
200	6,000	30
400	11,200	28
600	15,000	25
800	17,600	22
1,000	25,000	25
1,200	33,600	28

3. Answers may include the following:

- + The retailers that sell Cotton On Ltd's clothing are saying that they want more clothes to sell. By using outsourcing the company can increase its production very quickly. This would allow it to take advantage of the popularity of its clothing, which may not last forever, and achieve its objective of further growth.
- + The supplier that Cotton On Ltd is considering using is able to produce the items of clothing at the same price per item as the company itself. This suggests that the company's costs and profits will remain as they are, because its retailers are demanding that its prices are not increased when output rises.

4. Answers may include the following:

- + Producing the products itself will lead to Cotton On Ltd suffering from diseconomies of scale if it increases its output to 1,200 items a day. The data shows that its unit costs will rise from £25 to £28, so Cotton On Ltd would need to increase prices to keep profits per unit the same. The company's retailers want the same prices, so an increase in price could mean that its sales fall if some retailers stop selling its products.
- + Sales could rise if Cotton On Ltd chooses to use the supplier to outsource some of the production that is needed. This would allow it to avoid the diseconomies of scale that would result if it increases its own production beyond 800 items a day. The supplier is ready to produce up to 600 items, so has sufficient capacity.
- + Much depends on the quality of the supplier's clothing as Cotton On Ltd enjoys a good reputation for the quality of its products. However, the samples sent by the supplier have been excellent quality. On this basis, the company should use outsourcing as this will help it to grow by keeping its unit costs under control and its retailers happy.

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2.1 Technology

1. Answers may include two of the following:
 - + Email
 - + Webchat
 - + Social media such as Twitter and Facebook
2. Answers may include the following:
 - + ICT has affected the location of MPS Ltd's employees who manage the ICT system. They are all based in Leeds, rather than being scattered around the country at various stores. It may have helped in terms of staff efficiency as it is managed by a small team.
 - + The ICT has helped MPS Ltd to collect information about its customers. It holds a lot of information about its customers, and this can be analysed to help the company to take decisions on what to stock.
3. Answers may include the following:
 - + The use of digital communication has helped the company and its customers to communicate quickly and effectively. For example, customers use email and social media to enquire about buying the company's products online. This has allowed the company to respond almost immediately when required and to reach the correct people.
 - + The company has 47 suppliers and they are able to access the company's extranet. This allows them to communicate quickly about issues relating to supplies and to receive swift responses. This also means that the quality and rapidity of communication are much improved.
4. Answers may include the following:
 - + The company is profitable and by selling through its shops it is able to provide customers with advice as well as photographic services. This is a level of service that it cannot provide online and helps to distinguish the business from its larger competitors.
 - + MPS Ltd's customers clearly want to be able to buy products online. Online sales are rising and, if the company wants to turn around its recent fall in sales, creating a website is an obvious move.
 - + It would be a sensible decision to sell online. MPS Ltd clearly has a reputation for providing advice and local services, and this is perhaps the reason for its success. However, it can sell online alongside this. It is obviously what its customers want, so if it fails to do this it may lose further sales to larger competitors.

2.2 Ethical and environmental considerations

1. Global warming is the gradual heating of Earth's surface, oceans and atmosphere.
2. Answers may include the following:
 - + The company might buy its timber from supplies that do not grow timber sustainably. Some timber comes from overseas and the environmental costs of transporting it may mean that its use is not sustainable in the long term.
 - + The company transports its products throughout the UK. Its vehicles are likely to add to air pollution, as they deliver throughout the UK and travel long distances. They may also be caught up in congestion, adding further to air pollution.
3. Answers may include the following:
 - + The company could ensure that all its timber is sustainably grown. This means that the timber it uses is replaced with newly planted trees in a relatively short period of time. As a result, the company can be assured that it will not use up all the timber available to it.

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- + GA Ltd could also consider more environmentally friendly methods of transport. For example, it might decide to just use UK-based suppliers. This would mean that the timber would be transported shorter distances. This would lead to lower emissions of carbon and other gases. Timber is heavy and bulky, so this change could have a significant impact on the company's impact on the environment, enabling the industry to continue into the future.
4. Answers may include the following:
- + The company sells similar products to the other businesses that are in the same market. It also sells at similar prices. If GA Ltd adopts environmentally friendly methods of production this may increase its costs. As a result, its prices may have to be increased and its products may appear relatively expensive and less value for money. Sales may fall.
 - + The company could make its products more distinctive and different from those of its rivals if it became environmentally friendly. It could use this in its advertising and this might help it to attract and keep more customers. This may help to increase its sales, even if its prices are higher.
 - + Becoming an environmentally friendly company is an approach that may work as GA Ltd will probably struggle to increase sales with its current approach, especially as it is finding it difficult to keep costs low. The market is made up of many similar businesses, so being different may help it to achieve its aim of growth.

2.3 The economic climate of business

1. An overdraft is a flexible loan linked to a bank account which a business can use, whenever necessary, up to an agreed limit.
2. Answers may include the following:
- + Kiki may benefit from more people wanting to visit her hotel as there will be more people in employment and therefore able to spend money at the hotel.
 - + Kiki may find it increasingly difficult to hire people to work at the hotel as it is already a problem. She may also have to pay employees higher wages to prevent them leaving for other jobs.
3. Answers may include the following:
- + The rise in interest rates could affect Kiki's hotel because she borrowed a large sum of money to purchase the property. She has to make repayments on this loan and a rise in interest rates will increase the cost of these payments. The outcome could be a significant reduction in her profits.
4. Answers may include the following:
- + Rising incomes can benefit a business because they can expect to sell more products, especially if these are income elastic products which consumers buy in larger quantities when their incomes rise. This might be true of Kiki's hotel which has customers whose incomes are forecast to rise steadily over the next two years.
 - + Some businesses, however, may not see a rise in sales in these circumstances. Businesses that sell basic foods such as eggs and bread may find that their sales are stable when consumers are enjoying higher incomes. The extra income will be spent on other non-essential products, such as a stay at Kiki's hotel.
 - + It is not the case for all businesses. Some will benefit, but some may even suffer falling sales. For example, fewer people may travel on buses as rising incomes mean that they can afford to buy cars. Also, many businesses may have to pay higher wages so that consumers can have higher incomes.

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2.4 Globalisation

1. Quality is the extent to which a consumer is satisfied with a product.
2. Answers may include the following:
 - + Due to globalisation, supermarkets in the UK may be able to buy a wider range of products from different countries. They may also be able to find suppliers who charge lower prices, helping their profitability.
 - + UK supermarkets are facing increased competition from overseas rivals such as Lidl. This might result in lower sales and less profit if they lose customers to overseas supermarkets.
3. Answers may include the following:
 - + A fall in the exchange rate of the pound increases the cost of imported resources. Green Ltd imports a large quantity of resources from overseas. This will have a substantial effect on its costs of production and may make it more difficult to sell its products if it increases its prices. Green Ltd already sells at 'very high prices'.
 - + However, Green Ltd also sells overseas. The fall in the exchange rate of the pound will make Green Ltd's prices lower in overseas markets, for example in Europe. Although its costs of production may have risen, this may be offset by the lower prices of its meals when prices are converted from pounds to foreign currencies. This may help sales and profits.
4. Answers may include the following:
 - + Green Ltd may be able to design some new ready meals that would prove popular overseas. As it is a manufacturer of quality meals it could develop a range of classic British dishes, such as beef wellington, for sale to international customers. This may help it to win new customers who have not bought its products before or attract larger orders from existing customers already impressed by its quality. This could make it more competitive internationally.
 - + Alternatively, Green Ltd could focus on the quality and price of its products. Its ready meals are recognised as being quality products. If the company could reduce its prices a little this would make them better value for existing customers who may increase orders. This might also attract new customers. Both factors would increase its competitiveness against international rivals.
 - + The company should opt to use improved product design to enhance its international competitiveness. It has a reputation for quality products and cutting its prices might mean customers begin to doubt the quality of its products. It may also make it more difficult for Green Ltd to make a profit.

2.5 Legislation

1. Answers may include the following:
 - + Employees are protected against a dangerous working environment.
 - + Employees are given protective clothing to wear where required.
 - + Employees receive training in health and safety matters.
2. Answers may include the following:
 - + The company's consumers are protected against buying dangerous products – for example, a television that is electrically unsafe due to poor wiring or a radio which contains dangerous chemicals.
 - + Etal plc's customers who buy online are protected because the product remains the responsibility of the company until the consumer actually receives it. This protects against expensive items 'going missing'.
3. Answers may include the following:

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- + Most of Etal plc's employees are members of a trade union. Employment law gives employees the right to be members of a trade union. Etal plc's employees receive relatively high pay rates, which may be because they are supported by a trade union. Without this right, their standard of living might be substantially lower.
 - + Etal plc's employees are diverse and would therefore benefit from the Equality Act which protects them against discrimination. This means, for example, no group in the workforce can be treated any differently without good reason. As a result, everyone benefits from Etal plc's relatively high rates of pay.
4. Answers may include the following:
- + Etal plc benefits from the positive impact that employment and health and safety legislation has on the performance of its workforce. The company always conforms to relevant laws and its employees are loyal to the business. The company benefits from this in terms of having an efficient and loyal workforce. This means the company earns high levels of revenue and does not have to appoint many new employees.
 - + The company inevitably incurs higher costs of production because of this legislation. The company operates some production line equipment which has the potential to be dangerous. Health and safety law means that Etal plc has to spend heavily on protecting its employees from these dangers. At the same time its pay rates are higher than those in similar factories. This might be because many of its employees are members of a trade union. These high costs may lead to lower profits.
 - + Overall, the company may benefit from these laws. It helps it to have a happy and efficient workforce that is loyal to the business. This probably helps to make the company's products popular with UK consumers and boosts its profits.

2.6 The competitive environment

1. A business plan is a document setting out what a business does and what it hopes to achieve in the future.
2. Answers may include the following:
- + Kenton could face the risk of bad publicity if some of his beer was of poor quality. This might mean that his sales fall sharply.
 - + Kenton might not attract sufficient customers and even if he spends a large proportion of his £50,000 on advertising, this is a small sum alongside the advertising spending of multinational brewers.
3. Answers may include the following:
- + Kenton operates in a market which has a lot of small breweries selling similar products. This means that there is a lot of price competition, and it is difficult for the company to have lower prices than its larger rivals. Kenton has to try and make his beer different – and better – than that of his rivals.
 - + Globalisation has allowed some large multinational companies to enter the UK's beer market. They can produce a lot of beer and have well-known brand names. This can make it difficult for Kenton to compete as he would have to offer very low prices and spend heavily on promotion to do so directly. He cannot do this.
4. Answers may include the following:
- + Drawing up a business plan for the expansion would be an excellent idea for Kenton. He is worried and this might help to reduce his concerns, especially as an experienced entrepreneur has offered to help with the planning, which will reduce the risk of Kenton making further mistakes. If Kenton is to borrow £50,000, a business plan will be essential to persuade a bank

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to lend him the money. Without the loan, Kenton will be unable to pay for advertising which will increase his risks.

- + There are possible opportunities for Kenton to sell his beer in markets overseas as well as in the UK. This will help him to achieve higher sales as there are many potential customers overseas and this may reduce the risk of not attracting sufficient customers. It would also reduce the risk associated with an increase in the UK tax on beer.
- + However, there may not need to be a choice between using a business plan and selling in different markets. Kenton could do both, which would probably reduce his risks the most.

3 Business operations

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3.1 Production processes

1. Flow production takes place when an item moves continuously from one stage of production to another.
2. Answers may include the following:
 - + The company only produces two products – still and sparkling water. There is not much scope to alter these products to meet customers' needs.
 - + The company looks to control its costs carefully and this would not be possible if it was to use job production as it would increase its costs and therefore its prices.
3. Answers may include the following:
 - + The company produces huge quantities of bottled water for its customers and its sales are growing steadily. Flow production offers an ideal system under which to produce this volume of products at the lowest possible costs resulting in high profits – £400 million last year.
 - + The company makes use of technology to help keep its costs low and to increase its ability to produce increasing quantities of bottled water. Flow production enables the use of technology, and this is essential if the company is to continue to increase its output to match demand from its customers.
4. Answers may include the following:
 - + The company has been very successful in selling its products, partly because it has controlled costs and kept its prices low. Using lean production techniques to reduce waste will help the business to become more efficient and possibly to lower its prices further.
 - + Manuela plc uses a large number of suppliers from which it buys its bottles. This would make it more difficult for the company to operate a just-in-time stock control system. It would be easier for the company to operate this with one or two larger suppliers.
 - + There are clear benefits to the company in controlling waste and its costs. It may need to negotiate with its suppliers – and perhaps reduce their number – to make just-in-time production work. Overall, the company would be more likely to continue to increase sales and to make higher profits with the use of lean production.

3.2 The role of procurement

1. Logistics is the movement of goods, services, information and money throughout the production process.
2. Answers may include the following:
 - + Petra Ltd has never had any dealings with these two suppliers. They might not be reliable and production may have to be stopped if no supplies are available.
 - + Some of Petra Ltd's customers are very large businesses. If it cannot supply these customers because it does not have sufficient supplies of its own, it may lose their custom.
3. Answers may include the following:
 - + Petra Ltd would have had to consider the cost of buying from these suppliers very carefully. Its customers want to be able to buy cheaply, as price is very important to them. Petra cannot supply its customers cheaply if it has to pay its own suppliers' high prices and it wants to maintain its current level of profits.
 - + The new suppliers should be able to supply flexible quantities at very short notice. Petra Ltd is using a JIT system and has customers who demand varying quantities of products at short notice. The company's new suppliers must be sufficiently flexible to manage these circumstances.

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4. Answers may include the following:
 - + Price is very important for Petra Ltd's customers. If Petra Ltd can reduce its costs by holding little or no stock, then it is likely that it will be able to sell its fast fashion at lower prices. This might help the company to gain more sales, especially as its customers may order very large quantities.
 - + This decision may result in Petra Ltd losing its purchasing economies of scale as it will be placing a larger number of smaller orders. This could offset many of the other financial advantages associated with JIT stock control methods.
 - + This is a risky decision by Petra Ltd because it is using new suppliers, a new production and stock control system, and has a small number of customers who place large orders. If anything goes wrong, the consequences could be severe. It may be better to continue to hold some buffer stocks, at least in the short term.

3.3 The concept of quality

1. Outsourcing occurs when a business uses another business to produce products or provide a service for it.
2. Answers may include the following:
 - + The company's customers will expect to have a burglar alarm that is reliable and does not stop working when it is protecting their possessions.
 - + Customers will expect the burglar alarm to be effective and to work in most situations to prevent burglars entering a house or other property.
3. Answers may include the following:
 - + The company is not very profitable. If it has a large number of its alarms returned to the factory this will increase its costs as it will have to replace or repair them. In either case, this will involve increased spending and its already small profits may shrink further.
 - + The company wants to grow further. If its reputation is hit by increasing quality issues, existing customers will go elsewhere and not recommend Saracens. It will also become more difficult to win new customers, making it impossible to meet the company's objective of growth.
4. Answers may include the following:
 - + The company has received an increasing number of complaints about poor quality. Introducing TQM will help to overcome this by involving everyone in the business in inspecting the alarms and making sure that they meet agreed standards. This could reduce the number of complaints.
 - + Saracens Ltd does not have a lot of money to invest in training its employees to use TQM. The company is not profitable and unless it can train its employees to operate the system of TQM it is not likely to be successful, as they will not have the necessary enthusiasm or skills to make it work.
 - + The problem with quality has only occurred since Saracens Ltd started outsourcing its production. There may not be a problem with quality issues at the company's factory in Derby. It does not make sense to introduce TQM here when the problem is at the factory of the outsourcing company in Glasgow.

3.4 Good customer services

1. Answers may include the following:
 - + improving the product knowledge of its staff
 - + using communication technology such as Facebook and Twitter
 - + providing a more positive experience for the customer

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- + improving the product.
2. Answers may include the following:
- + The company may be able to attract more customers to travel on its services. If its reputation improves then more people might travel, increasing its revenue.
 - + Its customers may become more satisfied and, as a result, the government might agree to give it a new franchise in two years' time.
3. Answers may include the following:
- + The company may suffer a reduction in revenue. Commuters may decide to find other ways of getting to work, such as driving at least part of the way or using the bus instead. If this happens, the company may suffer a fall in revenue. This could be very damaging as its profits are already low.
 - + The government may decide against allowing Pagan plc to continue to provide rail services in this region. If customers are very unhappy with the level of service received, they may protest and the government would be under pressure to give the franchise to a different company. Pagan plc may not survive this, given its current weak financial position.
4. Answers may include the following:
- + It might be better for the company to focus on what causes the delays to the trains and the cancellations as providing a good product that meets customers' needs is a vital part of giving good customer service. Commuters need to arrive at work on time, and may not continue to travel with the company if this is not the case; improving ICT will not help with this.
 - + Part of the problem with Pagan plc's customer service is that it does not communicate with its customers effectively. Using social media, such as Twitter, would enable it to communicate with passengers and advise them of delays and the causes of them. This may help to improve customer service standards and increase customer loyalty.
 - + It would seem to be a good move for the company to use ICT to improve its customer service. It will not solve the entire problem but will at least ensure customers have up-to-date product information. This is not a costly move, which is important, given the company's low profits.

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4.1 Organisational structures

1. Answers may include the following:
 - + email
 - + intranet
 - + video-conferencing
 - + meetings.
2. Answers may include the following:
 - + The company is growing quickly and this will mean that spans of control might become wider and senior managers even busier. Delegation will help to overcome this.
 - + The company has decentralised and has moved away from using a 'standard' menu in each of its restaurants. Delegation will be necessary to support these changes and to ensure that they work.
3. Answers may include the following:
 - + The company's restaurants are located across the UK which would make it difficult for senior managers to supervise the work of subordinates closely and to communicate regularly with them as part of their management. As a result decisions may not be passed on and the restaurants may not operate efficiently
 - + Tall organisational structures are associated with close supervision, control by managers and little freedom for employees to make decisions. This management style would not fit with the chief executive officer's approach of allowing employees as much freedom as possible to make decisions.
4. Answers may include the following:
 - + The company's restaurant managers have wanted to make use of products that are available locally and not to follow a standard menu. Decentralisation will allow restaurant managers to take important decisions such as designing menus that reflect customers' tastes and the supplies that can be bought locally.
 - + The company's owners want its customers to have similar experiences in each of its restaurants. This will become more difficult if each restaurant manager makes individual decisions about an important issue such as the menu. It may result in products and standards of customer service varying between the restaurants.
 - + It is probably a good decision, as long as all managers work to the same guidelines. The restaurant is forecast to grow further and it will be more difficult for a few managers to make all the decisions if this happens.

4.2 Recruitment and selection of employees

1. Answers may include the following:
 - + job description
 - + person specification
 - + job advert.
2. Answers may include the following:
 - + Working part-time allows Zia to balance her family life with her work and to earn some income.
 - + Zia is content to work part-time at the moment. In the future she hopes for full-time work and promotion. Working part-time now allows her to gain skills and experience.
3. Answers may include the following:

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- + The company already has problems with staff retention. If it can improve its recruitment and selection process, this might help Charm Ltd to appoint suitable people. If the people appointed have the right skills and experience, these employees may be less likely to leave, helping the company to improve its control of costs.
 - + The company has suffered problems with the quality of its clothing. If it can employ more suitable and skilled employees, it may be able to produce clothing that meets the needs of its customers more fully. This should help it to reduce its costs and improve its profits.
4. Answers may include the following:
- + Charm Ltd is growing quickly and has already lost a number of talented employees. Many only stay a year or two. There may not be enough talented employees within the business to choose from, which might result in the business supplying poor quality products that do not meet customers' needs due to, for example, faults with the clothing or late delivery. This means that it is essential for the company to use external recruitment to bring in skilled employees to compete with its rivals.
 - + Using internal recruitment may be a good idea as it will provide some opportunities for promotion for employees already working at Charm Ltd. This might help to improve the company's retention of employees, as lack of promotion is a key reason for employees leaving the business. If the employees have been with Charm Ltd for a while, they may have sufficient knowledge and skills to ensure that products are fault-free and delivered promptly.
 - + Mitch thinks that they have not appointed suitable people. This could be a reason why the company is facing quality problems. Promoting them to more senior posts will be unlikely to improve the quality of the company's products. If Mitch is right, the company should use external recruitment as supervisors are able to influence decisions relating to quality.

4.3 Motivating employees

1. Answers may include the following:
- + profit sharing
 - + piece rate
 - + commission (for some employees)
 - + overtime.
2. Answers may include the following:
- + Raul might offer more training to his employees (they currently receive little) to enable them to carry out more complex tasks at work and make them feel valued.
 - + Raul could consider offering fringe benefits. For example, employees might be able to buy the company's sofas and chairs at a discount given they receive quite low pay.
3. Answers may include the following:
- + The company has low levels of employee retention as many do not stay long with the company. Improving the motivation levels of the workforce would help to persuade employees to stay, improving rates of staff retention. This would avoid the need to recruit new employees regularly and would reduce costs of recruitment and selection, as well the number of costly errors made by the workforce.
 - + Improving the motivation levels of the workforce should provide financial benefits for the business because recruitment and training costs would be lower as fewer new employees would be hired. This may mean that shareholders might get the higher profits they want.
4. Answers may include the following:
- + The company is profitable and its employees are paid a straight hourly rate, which is lower than that paid by another local business. Raul could think about offering another form of payment to

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add to the wages the employees already receive. A profit-sharing scheme may work in these circumstances.

- + The company's employees may be bored. They do not make any decisions and carry out simple tasks while being closely supervised. Raul could consider changing his management style to give the employees more freedom at work. Using job enrichment to make the employees' jobs more interesting and challenging might be a very effective way of helping to improve motivation levels in these circumstances.
- + The company's shareholders are hoping for higher profits. Using financial methods of motivation is likely to reduce the profits of the company in the short-term, and displease the shareholders. Furthermore, the jobs carried out by the employees appear dull, which is possibly why many do not stay long. These are good reasons to recommend using non-financial methods of motivation.

4.4 Training

1. Induction training is the training given to an employee when they first start work in a new job.
2. Answers may include the following:
 - + Induction training makes it easier for new employees to understand the systems and approaches used at Benly Ltd and to be efficient in using production technology quickly.
 - + Induction training helps to make the employees feel more secure as they are supported in the early days of their new jobs and this perhaps explains high staff retention levels.
3. Answers may include the following:
 - + The company's employees enjoy working at Benly Ltd. Many of its employees are long-serving, partly because they receive training and feel valued by the company. This benefits the company because it retains its experienced employees and does not have to spend money recruiting large numbers of new staff due to employees leaving.
 - + Benly Ltd has a reputation for producing good-quality products that meet the needs of consumers. In part, this is a result of providing training for its employees. Having loyal and long-serving employees helps to maintain quality as employees are experienced, which can improve sales and therefore financial performance.
4. Answers may include the following:
 - + The company has a number of skilled and highly experienced employees who would be able to provide on-the-job training for the new employees. As the company has a reputation for high-quality products, these employees might be in a good position to provide the right training.
 - + The company wants to produce new products and to improve productivity levels. Its managers recognise that some new ideas are needed if it is to achieve these aims. Off-the-job training would offer opportunities to develop new ideas and approaches, and not to just continue in the same ways.
 - + The company is recruiting shop-floor workers and managers. It could use on-the-job training for its shop-floor employees as much of the company's work is excellent and it has a good reputation. Off-the-job training for the new managers might be a good way to bring new ideas and approaches into the company.

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Exam practice answers

5.1 Identifying and understanding customers

1. Answers may include the following:
 - + bread and milk
 - + gas and electricity
 - + petrol
 - + housing – mortgage or rent.
2. Answers may include the following:
 - + Blanch plc's adult consumers will need product information about its high-technology toys. Without this they will not know if the toys will be suitable to meet their children's needs.
 - + The technological toys sold by Blanch plc have sometimes needed to be repaired. Customers will need an after-sales service.
3. Answers may include the following:
 - + Blanch plc manufactures products that are fashionable and it must understand the needs of its customers in order to develop the latest toys. Fashions can change and the company has used its knowledge of its customers to produce the right toys, therefore attracting customers. As a result, its sales should continue to rise.
 - + Understanding its customers has helped Blanch plc to provide good value for money. If the company knows exactly what its customers want in terms of technology and fashion in terms of toys, it can meet these needs. This means it will provide more benefits to customers, giving increased value for money and helping to increase sales.
4. Answers may include the following:
 - + Blanch plc faces competition from many competitors, some of whom sell at lower prices. These companies are successful and it may help Blanch plc to reduce its prices so that its products are even better value for money. This might help it to attract customers away from its rivals.
 - + The company has a reputation for producing products that are up to date and fashionable. This means that they offer many benefits to customers and the fact that sales have been rising steadily suggests that consumers are happy with Blanch plc's prices.
 - + Reducing prices would improve the value for money received by the company's customers. However, the company only makes a small amount of profit and it may not be able to afford to reduce its prices. If it does it may not be able to provide products that meet the needs of its customers so fully. Blanch plc should not reduce its prices.

5.2 Segmentation

1. Answers may include the following:
 - + It could measure the quantity of products sold.
 - + It could measure the value of sales.
2. Answers may include the following:
 - + The company could segment its market by gender because men and women are unlikely to wear the same perfumes or aftershaves.
 - + It could segment its market by income as the company's exclusive and high-priced products are targeted at consumers with high incomes.
3. Answers may include the following:
 - + By segmenting its market and then producing a wider range of products aimed at different segments in the market, the company could expect to increase its sales. It is meeting the needs

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of more customers in the market by segmenting in this way. By satisfying these needs, the company will expect to attract more customers and to make more sales.

- + The company's profits may be higher as a result of segmentation. Through segmentation it is identifying customers who are willing to pay higher prices for more exclusive products. These sales could be very profitable. By selling cheaper products in large quantities, this may also add to its profits. Overall, the effect on the company's finances could be very positive.

5.3 The purpose and methods of market research

1. Answers may include the following:

- + questionnaires
- + surveys
- + focus groups.

2. Market share = $\frac{£690 \text{ million}}{£25,102 \text{ million}} \times 100 = 2.75\%$

3. Answers may include the following:

- + The company needs to identify what is happening to the level of demand for hotels in Edinburgh to be able to judge whether there will be sufficient sales and revenue to make the project profitable. It has grown recently, but will this continue? The company could use primary market research methods to discover this.
- + The company will be facing more competitors in the hotel market in Edinburgh. There were 42 companies in the market last year, but next year this is expected to rise to 51. Kvos Ltd needs to investigate this so that it can understand what the more successful of these companies are doing and whether it could do something similar. This would help it to judge whether buying the hotel would be a good decision.

4. Answers may include the following:

- + The company is under pressure to make a quick decision as other businesses are interested in buying the hotel. This could mean that it would make sense to use secondary methods of market research. These can be conducted quickly as they rely on existing information, rather than collecting new data.
- + The hotel market in Edinburgh is changing in two important ways. New hotel companies are entering the market and consumers' needs are changing. This means that secondary research is likely to be out of date and may not reflect what consumers want. This suggests Kvos Ltd should use primary methods of market research to find out what is happening in the market now.
- + Buying the hotel in Edinburgh needs a big investment by the company. It is important that the market research is right to enable the company's managers to make the most informed decision possible. Therefore, primary research should be carried out.

5.4 Elements of the marketing mix

1. An extension strategy is an attempt to maintain the sales of a product and to prevent it from entering the decline stage of its product life cycle.

2. Answers may include the following:

- + The Roman Blend range had suffered from falling sales and using an extension strategy might help to stop sales falling too quickly or too much.
- + The company is planning to launch its new cold-brew coffee next year. Keeping its sales of Roman Blend as high as possible for as long as possible is important at this time.

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3. Answers may include the following:

- + The company has generated high profits for many years from selling its Roman Blend range of coffee. This product has operated as a cash cow for some time, generating significant profits. This would provide the company with the funds needed to pay for heavy advertising for its new cold-brew coffee.
- + GC plc wants to replace a popular coffee product which has achieved very high sales. The new product is unique and offers plenty of benefits (sweeter, more recipes) to coffee drinkers. A high level of promotion will be necessary to inform coffee drinkers of these benefits and to remind them of these once the product has entered the market.

4. Answers may include the following:

- + Using cost-plus pricing will ensure that the company makes a profit from selling each cold-brew coffee product. However, it is possible the company could have charged higher prices for the cold-brew coffee product as coffee drinkers may have valued this new product highly.
- + Price skimming could be an appropriate pricing method as this is a new product with many benefits. This product will be appealing to some coffee drinkers, especially as they will not be able to buy the same coffee products elsewhere.
- + Price skimming may be the better choice because of the benefits offered by the coffee and the investment of millions of pounds in the products. It will give the chance of higher profits as prices can be set very high and reduced when competitors launch similar products.

6 Finance

Exam practice answers

6.1 Sources of finance

1. The interest rate is the cost of borrowing money or the reward for saving money, expressed as a percentage.
2. Answers may include the following:
 - + Using sale and leaseback means that the company would have to pay for a lease if it wanted to continue using the offices, increasing its costs of production.
 - + The company cannot always pay its existing bills without using its overdraft. Paying for a lease would add to these problems.
3. Answers may include the following:
 - + The company is sometimes short of cash to pay its bills. An overdraft is an effective means of dealing with this as it is flexible and can be used when necessary. Without an overdraft, the company might need a permanent loan, which might prove more costly and could damage the company's profits. This would make it more difficult for PH Housebuilders to raise further finance through a loan or a share issue.
4. Answers may include the following:
 - + A share issue takes place when a company sells shares to people, giving them part ownership of the business in return for payment. The company could issue new shares to finance the purchase of the land. This would be easier as it is a public limited company and it could sell its shares on the Stock Exchange. The company is popular with shareholders as it pays good dividends, which might mean that its new shares would be attractive to shareholders. This might make it easier to raise the finance that is needed.
 - + A mortgage is possible as the finance is needed to buy land. The land could be used as collateral for the mortgage, although the company would have to pay interest on the loan. As the mortgage would be for £9.5 million, the amount of interest paid would be quite large, which could cause problems for the company given its need to use its overdraft regularly.
 - + The new share offer seems more attractive for the business as it would avoid the need to pay interest. The company could share its profits with its shareholders, but this would only happen when, and if, it made a profit.

6.2 Cash flow

1. The net cash flow shows the balance of cash flowing into and out of the business over the month.

2.

	Next month	The month after next
Opening balance	(1,500)	(3,075)
Closing balance	(3,075)	(5,076)

3. Answers may include the following:
 - + The closing balance for the business is negative in both months. This means that some of the business's cash outflows are taking place before the equivalent inflows. Therefore, the business may have difficulties paying its bills as they become due. The business may be at risk of failing due to a shortage of cash and an inability to pay its bills on time.
 - + The closing balance has a larger negative balance in the second month. The business could be facing increasing cash-flow problems. This increases the risk of the business not being able to pay its bills sometime in the future, especially if this trend continues.

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4. Answers may include the following:

- + An overdraft is a possibility as Phil has a good record with his bank of repaying loans. However, his business's cash position has been getting worse for nine months and an overdraft is better suited to a short-term problem. This could be a very expensive choice as he would be using it every month.
- + Increasing his cash inflows by raising the business's prices could improve Phil's cash position by having larger inflows and the same outflows. This could be effective as his prices are very low and so his customers may not stop buying his products even if their price increases.
- + Increasing cash inflows by raising prices seems to be a better option. An overdraft is expensive and not really suitable for use in the long term when the business is only making a very small profit. This is the recommended option.

6.3 Financial terms and calculations

1. Answers to be two of the following:

- + fixed cost line
- + variable cost line
- + total cost line
- + revenue line.

2. Average annual profit = $\frac{£6,000}{5} = £1,200$

$$\text{Average rate of return} = \frac{£1,200}{£10,000} = 12\%$$

3. Answers may include the following:

Angie could increase her prices, especially as she thinks that they are probably too low. This would increase her business's revenue if she did not lose too many sales as the increased price per unit would more than compensate for the loss revenue from sales. Provided her costs do not increase, she should receive higher profits in these circumstances.

Angie doesn't open her café at the weekends. This could be a reason why her profits are low as a large number of people may visit the town at the weekends. If she opened on Saturdays and Sundays, she might receive more revenue and more profits, as she is likely to attract a substantial number of new customers.

4. Answers may include the following:

- + Angie knows that she will need a bank loan. If the bank knows that she has carried out a break-even analysis it may be more willing to lend her the money for the investment. This is because it may be more confident that the expanded café will make a profit in the future and be able to repay the loan.
- + The café may be larger but that doesn't mean that its sales will rise. Angie 'hopes' that sales will increase, but this may not happen. It is very unlikely to happen if she does not open the café at the weekends.
- + Break-even analysis might help Angie to decide whether or not to make this investment. It could show how many customers she will need in order to make a profit from the larger café. However, it doesn't mean that she will definitely increase sales and so make a profit. She should also carry out some market research to find out how many people might visit the enlarged café – especially if it opens at weekends.

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Exam practice answers

6.4 Analysing the financial performance of a business

1. Answers may include two of the following:

- + non-current assets
- + current assets
- + current liabilities
- + non-current liabilities.

2. Gross profit margin = $\frac{144,900,000}{804,800,000} \times 100 = 18\%$

Net profit margin = $\frac{£80,500,000}{£804,800,000} \times 100 = 10\%$

3. Answers may include the following:

- + The data only refers to the last year of trading for the two companies. It would be better to have the financial performance of each company over a number of years so that trends could be analysed. This would provide some perspective for the more recent performances.
- + This is an industry with many other businesses because both companies face a lot of competition. It would be very useful to compare their financial performance over time with their major rivals as well as having some industry information, so that the companies' performances could be judged against that of the market overall.

4. Answers may include the following:

- + HJK plc is a much larger company and achieved a much higher level of sales – more than 30 times that recorded by Brett plc. Its profits are also much higher; its net profit is over £80 million compared to under £3 million for Brett plc.
- + Brett plc is smaller and achieved fewer sales and lower profits. However, the results of the financial ratios show that the company's profit margins were both higher than those of HJK plc. Its GPM was 2% higher and its NPM 1% higher. On this basis, its financial performance is better.
- + It is probably true to say that Brett plc performed better due to its superior profit margin figures. However, there is very limited information on which to make a judgement of this type.